Mariner
WEALTH ADVISORS

How to Strategically Fund Long-term Care

Seven out of 10 people who turn age 65 will need long-term care during their retirement, and 20% will need it for more than five years.[1] How will you fund it? At Mariner Wealth Advisors, we can model estimated cost of care for your situation to determine whether it makes sense for you to fund it from personal investments, a permanent life insurance policy or from an annuity.

If you plan to explore the strategic use of a life insurance policy or annuity to pay for long-term care, we'll explain how each of those work and what to consider as you weigh your options.

How Does a 1035 Exchange Work?

Similar to a 1031 exchange for real estate, a 1035 exchange allows you to convert a life insurance policy or annuity into another insurance product of "like kind." Additionally, the owner and insured/annuitant of the new policy must be the same as the old policy. This process does require proof of insurability. If you meet the IRS requirements for the exchange, you won't pay tax on any gains associated with the original policy.

For example, you could use a variable annuity that may have built up significant gains and take all or part of it (called a partial 1035 exchange) and convert it into an annuity with long-term care (LTC) benefits. It's the only way you can access gains from an annuity income tax free, assuming you meet IRS requirements.

One of the IRS requirements for any 1035 exchange is that it has to be a direct exchange between insurance companies, versus an individual receiving a distribution from one insurance policy or annuity and then using it to purchase another one.[2]

In the case of an exchange, you would still be the one insured by the policy, but you would be able to change the beneficiary. Your older policy may be subject to a surrender charge, which is a charge you incur for canceling an insurance or annuity contract within the surrender period. Your wealth team can help you understand the impact of an exchange.[3]

Is a 1035 Exchange Right for You?

Your age and health are key factors that help determine whether using a 1035 exchange to fund long-term care is right for you. One benefit is that you trade an outdated insurance policy or annuity that no longer meets your needs for one that can help fund long-term health care and meet your asset protection needs.

Depending on the monthly benefit you seek, it's also possible to pay a single premium at the time of the 1035 exchange to achieve your long-term care policy payout goal. Because this type of strategy is complex, it's a good idea to work with your wealth team to decide what's right for you.

How Does Adding a Rider to a Policy Work?

The tax code allows you to fund new, permanent insurance policies with long-term care or chronic illness riders from the values of older polices that might otherwise trigger income tax if surrendered.

Essentially, the payments you receive from the rider are subtracted from your policy's death benefit each month to pay for long-term care expenses. Keep in mind, when you're ready to access the rider, a medical professional would have to certify that you can't perform at least two "activities of daily living" on your own, such as preparing meals or dressing, or that you need significant supervision to be safe due to a cognitive decline. You may also have a 90-day waiting period before receiving benefits.

Is Adding a Rider Right for You?

You typically add a LTC rider when you are issued a new, permanent life insurance policy. There are limited circumstances where it could be added to a current permanent life insurance policy, so be sure to consult with your wealth team on your specific situation.

Adding a rider can be a more cost-effective option than purchasing a traditional LTC insurance policy. Should you not use the rider during your lifetime, your beneficiaries would receive the full death benefit payout from your policy, less what you owe on policy loans.

Our risk management team often recommends strategies that allow for full cost recovery, if not used. All the premiums you pay will come back to the family in the form of the death benefit or LTC benefit. If you do use the rider during your lifetime, then the policy's death benefit payout to beneficiaries would decrease, in most cases, dollar for dollar. Also, the LTC rider will have a monthly and lifetime maximum long-term care benefit.[4]

Consult With Your Wealth Team

At Mariner Wealth Advisors, your wealth advisor will work closely with our in-house risk management team to help you decide how best to fund long-term care costs in retirement. Our risk management professionals can also evaluate your existing insurance policies and annuities that you may not have reviewed in a while and recommend whether or not to repurpose those to align with your financial goals, including funding long-term care.

For more information visit: marinerwealthadvisors.com

Sources

1 "How Much Care Will You Need?"
2 "What Is a Tax-Free 1035 Exchange?"
3 "How a 1035 Exchange Works"
4 "Long-Term Care Rider"